

AR78

2004

ANNUAL REPORT

Saxon Energy Services Inc.



AN INTERNATIONAL
ENERGY SERVICES COMPANY

Saxon Energy Services Inc.

CORPORATE PROFILE

Saxon Energy Services Inc. (the "Company") is an emerging oilfield service company engaged in providing oil and gas drilling, completion and workover services to its clients. By leveraging its operations in Ecuador and Venezuela, the Company plans to pursue an aggressive growth strategy through the consolidation of existing companies operating in its area of interest, and the acquisition of complementary operating assets. The common shares of the Company trade on the Toronto Stock Exchange (TSX) under the symbol SES.

NOTICE OF ANNUAL GENERAL MEETING

The Annual General Meeting of the shareholders of Saxon Energy Services Inc. will be held on Wednesday, May 18, 2005 at 10:00 am (local time) in the Royal Room of The Metropolitan Conference Centre, 333 - 4th Avenue S.W. Calgary, Alberta, Canada.

Saxon Energy Services Inc.

President's Message

2004 was a year during which Saxon Energy Services Inc. (the "Corporation") took major strides towards its goal of becoming a significant international oil and gas service company concentrating in Latin American markets.

Ecuador

The Corporation was formed in December 1995 and completed the acquisition of Perforec, an Ecuadorian company with 5 service rigs, in September 2000. Subsequent to the acquisition, in fiscal 2002, 2 additional workover rigs were added to the fleet. During fiscal 2004, the Corporation invested US \$12.7 million in the construction of 3 new dual workover/drilling rigs. Two of these rigs were deployed in the fourth quarter and the third is expected to commence operations in May 2005. These additions, together with higher utilization rates caused by higher oil prices, will combine to boost revenues from Ecuador from US \$15.1 million in 2004 to a forecast US \$19.0 to US \$22.0 million in 2005. Ecuador is seen as a key growth market for the Corporation as oil and gas remain Ecuador's largest export and there is surplus pipeline capacity to be filled. The high demand for rigs should allow the Corporation to achieve improved utilization as contracts for up to 2 years are now becoming more frequent and operators increasingly prefer modern equipment operated with the high safety and environmental standards delivered by the Corporation.

Venezuela

The Corporation entered the Venezuelan arena on January 4, 2005 with the closing of the purchase of Justiss Drilling de Venezuela for US \$18.5 million. The purchase adds 4 drilling and 7 workover rigs to the Corporation's fleet and 2005 expansion plans include the addition of 4 drilling rigs and certain rental equipment to the Venezuelan operation. Justiss generated revenues of US \$15.4 million for the year ended November 30, 2004 and the planned equipment additions combined with higher utilization are forecasted to increase Venezuelan revenues to US \$33.5 to US \$38.0 million in 2005 assuming that the construction timetable can be met. As in Ecuador, hydrocarbons are Venezuela's principle export and demand for drilling and workover rigs is anticipated to be very strong in 2005. The country, through PDVSA the state owned oil company, is committed to restoring the production lost in the 2001 to 2003 slowdown thus driving the demand for drilling services.

Financings

Between June and August 2004, the Corporation closed a private placement of common shares and warrants totaling US \$9.4 million net of costs. In January, 2005 the Corporation completed a further private placement of common shares and warrants for gross proceeds of US \$40.6 million. Both equity financings included the issue of share purchase warrants with exercise terms from 9 to 18 months which should provide additional funds for capital projects through June 2006.

In January 2004, the Corporation received a shareholder loan of US \$6.0 million which was used to repay existing term debt and finance capital expenditures. The outstanding balance of this loan was in turn repaid in January 2005 from the proceeds of the private placement.

After the reverse takeover amalgamation with Consolidated Epix Technologies Limited, the Corporation was listed on the TSX and commenced trading under the symbol "SES".

Strategy

Geographically, the Corporation intends to focus its activities outside Canada and the USA as these areas have seen considerable consolidation within the drilling and service rig sectors over the last two decades. By contrast, such consolidation has not occurred in areas such as Latin America and North Africa and the equipment available is often poorly maintained. Large oil companies increasingly demand better equipment and higher safety and environmental standards than are currently available in these areas. The Corporation's objective is to provide first class equipment with well-trained local personnel to meet these requirements. The Corporation will concentrate on the acquisition of dual purpose rigs (capable of economically providing both workover and drilling services) in the mid-horsepower range up to 1800 hp with the capability of rapid rig up and rig down and ease of transportation. The ability to perform workover operations is key to ensuring continuing utilization after the drilling is completed. Acquisitions will be made of existing businesses or by construction of new equipment as the opportunities merit.

In keeping with this strategy, the Corporation has embarked on a major two-pronged asset acquisition program which, when completed, will approximately double its business assets in its geographic target market in South America. First, the Corporation has entered into a detailed letter of intent to acquire additional drilling rigs and has commenced the process for the building of additional new drilling rigs and refurbishing a further drilling rig for a total of 10 drilling rigs. These rigs will be deployed in the Corporation's target geographic markets in South America.

The drilling rig purchases are subject to definitive documentation, regulatory approval and completion of final due diligence and finalizing the specs on the new builds. The acquired rigs will expand the Corporation's long established, existing Ecuador and Venezuela operations and commence new operations in strategic Latin American markets. The closing for the first phase of drilling rigs is planned for the end of April 2005 while the construction and refurbishing of the remaining rigs is expected to begin in the second quarter.

Second, the Corporation has commenced the process of acquiring approximately US\$16 million worth of rental drilling equipment (top drives, drill strings, collars and related drilling rental equipment) to complement its pro-forma, 35-rig operation. The rentals acquisition is expected to be completed in the second quarter. The total cost of these two initiatives will be approximately US\$74 million. These initiatives are expected to add incremental revenue in fiscal 2005 of US \$28 million to US \$32 million assuming that the acquisition and construction timetable can be met.

On March 23, 2005, the Corporation entered into an agreement for bought-deal private placement for gross proceeds of CDN \$80.0 million which will be used in part to finance the aforementioned expansion. The private placement is scheduled to close prior to April 7, 2005,

In conclusion, I would like to thank our employees for their hard work and dedication. I look forward to a year of exciting opportunities for the Corporation.

On behalf of the Board of Directors,



Walter Dawson

President & C.E.O.

Ecuador and Venezuela – A Platform for Growth



Saxon Energy Services Inc.

Disclosure Regarding Forward Looking Statements

Certain statements contained in this Report, including statements which may contain words such as "could", "plans", "should", "anticipates", "expect", "believe", "will", and similar expressions and statements relating to matters that are not historical facts are forward-looking statements including, but not limited to, statements as to: future capital expenditures, including the amount and nature thereof; drilling activity levels; oil and gas prices and demand; expansion and other development trends of the oil and gas industry; improvement in day rates; business strategy; expansion and growth of Saxon Energy Services Inc.'s ("the Corporation") business and operations, including the Corporation's market share and other such matters.

These statements are based on certain assumptions and analyses made by the Corporation in light of its experience and its perception of historical trends, current conditions and expected future developments as well as other factors it believes are appropriate in the circumstances. However, whether actual results, performance or achievements will conform with the Corporation's expectations and predictions is subject to known and unknown risks and uncertainties which could cause actual results to differ materially from the Corporation's expectations, including: fluctuations in the price and demand of oil and gas; fluctuations in the level of oil and gas exploration and development activities; fluctuations in the demand for the Corporation's services; the existence of competitors, technological changes and developments in the oil and gas industry; the ability of oil and gas companies to raise capital; the effects of severe weather conditions on operations and facilities; the existence of operating risks inherent in the Corporation's services; identifying and acquiring suitable acquisition targets on reasonable terms; general economic, market or business conditions, including stock market volatility; changes in laws or regulations, including taxation and environmental regulations; the lack of availability of qualified personnel or management; and other unforeseen conditions which could impact on the use of services supplied by the Corporation.

Consequently, all of the forward-looking statements made in this Report are qualified by these cautionary statements and there can be no assurance that the actual results or developments anticipated by the Corporation will be realized or, even if substantially realized, that they will have the expected consequences to or effects on the Corporation or its business operations. The Corporation assumes no obligation to update publicly any such forward-looking statements, whether as a result of new information, future events or otherwise.

Saxon Energy Services Inc.

Management's Discussion and Analysis

This Management Discussion and Analysis has been prepared taking into consideration information available to March 23, 2005. This discussion focuses on key statistics from the audited Consolidated Financial Statements and pertains to known risks and uncertainties relating to the oilfield services industry. This discussion should not be considered all-inclusive, as it excludes changes that may occur in general economic, political and environmental conditions. Additionally, other elements may or may not occur which could affect Saxon Energy Services Inc. ("the Corporation") in the future. This discussion also includes various forward-looking statements regarding the Corporation's markets, the demand for the Corporation's services and the Corporation's future results. These statements are based on certain assumptions that are considered reasonable by management. Prospective investors are cautioned that any such forward-looking statements are not guarantees of future performance and involve a number of risks and uncertainties and actual results could differ materially from those indicated by such forward-looking statements. This discussion and analysis of the financial condition and results of operations for the year ended December 31, 2004 should be read in conjunction with the Interim Consolidated Financial Statements for the nine months ended September 30, 2004, and the October 28, 2004 Joint Management Information Circular of Consolidated Epix Technologies Limited and the Corporation which contains the Interim Consolidated Financial Statements for the six months ended June 30, 2004 and the Audited Consolidated Financial Statements for the year ended December 31, 2003 and related notes and material therein. All amounts are expressed in U.S. dollars, unless otherwise indicated.

Highlights:

Stated in thousands of U.S. dollars, except per share amounts and operating data	Three Months Ended			Year Ended		
	December	December	Change	December	December	Change
	31, 2004	31, 2003	%	31, 2004	31, 2003	%
	(unaudited)			(audited)		
Revenue	4,504	2,706	66	15,062	11,866	27
EBITDA (1)	671	39	1621	2,415	1,740	39
Net earnings (loss)	184	(266)	n/a	652	156	318
Earnings (loss) per share						
Basic	\$ 0.01	\$ (0.04)	n/a	\$ 0.05	\$ 0.02	150
Diluted	\$ 0.01	\$ (0.04)	n/a	\$ 0.05	\$ 0.02	150
Funds from (used in) operations (2)	570	(77)	n/a	1,869	905	107
Funds from (used in) operations per share						
Basic	\$ 0.03	\$ (0.01)	n/a	\$ 0.14	\$ 0.12	17
Diluted	\$ 0.03	\$ (0.01)	n/a	\$ 0.13	\$ 0.12	8
Weighted average shares ('000's)						
Basic	20,059	7,446	169	13,814	7,816	77
Diluted	20,163	7,446	171	13,880	7,816	78
Utilization						
Operating hours	13,272	8,419	58	49,523	41,379	20

Notes:

- (1) Earnings before Interest, Tax and Depreciation ("EBITDA") is not a recognized measure under Canadian Generally Accepted Accounting Principles (GAAP). Management believes that in addition to net earnings, EBITDA is a useful supplemental measure as it provides an indication of the results generated by the Corporation's principal business activities prior to consideration of how those activities are financed or how the results are taxed in various jurisdictions. Investors should be cautioned, however, that EBITDA should not be construed as an alternative to net earnings determined in accordance with GAAP as an indicator of the Corporation's performance. The Corporation's method of calculating EBITDA may differ from other companies and accordingly may not be comparable to measures used by other companies. EBITDA is calculated as earnings before income taxes plus interest expense plus depreciation on property and equipment plus other expenses plus or minus any loss or gain on foreign exchange.
- (2) Funds from (used in) operations is not a recognized measure under Canadian Generally Accepted Accounting Principles (GAAP). Management believes that in addition to net earnings, Funds from (used in) operations is a useful supplemental measure as it provides an indication of the cashflow generated by the Corporation's principal business activities. Investors should be cautioned, however, that Funds from (used in) operations should not be construed as an alternative to net earnings determined in accordance with GAAP as an indicator of the Corporation's performance. The Corporation's method of calculating Funds from (used in) operations may differ from other companies and accordingly may not be comparable to measures used by other companies. Funds from (used in) operations is calculated as net earnings plus or minus future income taxes, plus depreciation on property and equipment, plus or minus the loss or gain on disposal of property and equipment, plus or minus any stock-based compensation expense, plus or minus any unrealized loss or gain on foreign exchange.

Saxon Energy Services Inc.

Overview:

The Corporation generated earnings before income taxes during 2004 of \$948,000 compared to \$364,000 in 2003, an improvement of 160%. The primary reasons for this improvement are: a 20% increase in rig operating hours in 2004 to 49,523 from 41,379 in 2003; higher average day rates in 2004 compared to 2003, the deployment of 2 new combination drilling/workover rigs in the fourth quarter of 2004; and a reduction in other expenses in 2004 from 2003.

The effective tax rate in 2004 was 31.2% compared to 57.1% in 2003. This reflects a decline in the Canadian statutory tax rate in 2004 and its effect on the tax assets of the Corporation, a decline in the amount of non-deductible expenses for tax purposes in Ecuador in 2004 compared to 2003, and the reclassification of Ecuadorian statutory profit-sharing provisions to operating expenses which reduced the effective Ecuadorian tax rate from 36.25% to 25%.

As a result, net earnings improved by 318% to \$652,000 (\$0.05 per share) during 2004 compared to net earnings of \$156,000 (\$0.02 per share) in 2003.

Revenue:

	2004	2003	Change	
Stated in thousands of U.S. dollars	\$	\$	\$	%
Revenue	15,062	11,866	3,196	27

For 2004, the Corporation generated revenues of \$15.1 million, a 27% increase over the \$11.9 million generated in 2003. The increase of \$3.2 million is due primarily to a 20% increase in rig operating hours to 49,523 in 2004 compared to 41,379 in 2003 combined with higher average day rates in 2004 compared to 2003. In addition, the deployment of 2 new combination drilling/workover rigs in the fourth quarter of 2004 accounted for 32% of the increase in operating revenues.

Direct Operating Expenses:

	2004	2003	Change	
Stated in thousands of U.S. dollars	\$	\$	\$	%
Direct operating expenses	10,050	8,520	1,530	18

Direct operating expenses increased by 18% during 2004 to \$10.0 million compared to \$8.5 million in 2003. The increase of \$1.5 million is due primarily to an increase in activity between the two periods. However, the increase in rig operating hours to 49,523 in 2004 compared to 41,379 in 2003 combined with an increase in the average day rate caused the fixed component of the Corporation's direct costs to decrease in proportion to its variable component. Therefore, direct costs in aggregate did not increase in direct proportion to revenues.

General and Administrative Expenses:

	2004	2003	Change	
Stated in thousands of U.S. dollars	\$	\$	\$	%
General and administrative expenses	2,180	1,583	597	38

General and administrative expenses increased by 38% to \$2.2 million in 2004 compared to \$1.6 million in 2003. The increase of \$597,000 is due primarily to the establishment of a formal corporate head office in Calgary, Canada, increased travel costs and increased administrative wages in Ecuador.

Saxon Energy Services Inc.

Public Listing Costs:

	2004	2003	Change	
Stated in thousands of U.S. dollars	\$	\$	\$	%
Public listing costs	259	Nil	259	100

Costs of \$259,000 were incurred in conjunction with the reverse-takeover transaction described in the October 28, 2004 Joint Management Information Circular of Consolidated Epix Technologies Limited and the Corporation.

Stock-Based Compensation Expense:

	2004	2003	Change	
Stated in thousands of U.S. dollars	\$	\$	\$	%
Stock-based compensation expense	157	Nil	157	100

Stock-based compensation expense represents charges to income in respect of the Corporation's stock option program and the issue of common shares and share purchase warrants as compensation to third parties for services rendered to the Corporation.

Between July 1 and August 30, 2004, the Corporation issued 210,000 common shares from treasury primarily issued as compensation to certain parties for the recruitment of investment capital into the Corporation.

The Corporation has estimated the fair value of the 210,000 common shares to be \$2.00 per share. The Corporation has recorded the fair value as follows: a charge of \$300,000 to share issue costs, a charge of \$120,000 to stock-based compensation expense, and a credit to share capital of \$420,000.

In addition, the Corporation's Board of Directors approved the issue of 1,675,000 stock options to the executives and directors of the Corporation. The Corporation has accounted for the issue of these stock options using the fair value method which resulted in a charge to stock-based compensation expense of \$33,000 in December 2004.

Depreciation and amortization:

	2004	2003	Change	
Stated in thousands of U.S. dollars	\$	\$	\$	%
Depreciation of property and equipment	1,072	664	408	61

Depreciation expense increased by 61% during 2004 to \$1.1 million compared to \$664,000 in 2003. The increase of \$408,000 is primarily the result of increased operating utilization of the Corporation's rig fleet, which is the basis for calculating depreciation, combined with the incremental capital expenditures of \$16.4 million that were incurred during 2004.

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Interest Expense:

	2004	2003	Change	
Stated in thousands of U.S. dollars	\$	\$	\$	%
Interest on term loan	11	265	(254)	(96)
Interest on shareholder advances	281	36	245	681
Interest on bank debt	64	44	20	45
	356	345	11	3

Interest expense on the term loan declined in 2004 compared to 2003 due to the fact that the term loan was repaid in full in January 2004.

Interest expense on shareholder advances increased substantially to \$281,000 during 2004 compared to \$36,000 in 2003. The increase is due to the interest-bearing shareholder advance of \$6.0 million, the proceeds of which were received in January 2004. In June 2004, \$4.2 million of the loan was converted into 4,540,463 (1,059,000 pre-split) common shares of the Corporation at a price of \$0.93 per share (\$4.00 per share pre-split).

Interest on bank debt increased by 45% to \$64,000 during 2004 compared to \$44,000 in 2003. The increase is due to the increase use of secured bank debt in 2004 compared to 2003. The increased use of bank debt and the associated interest was offset by slightly lower interest rates.

Foreign Exchange Loss:

	2004	2003	Change	
Stated in thousands of U.S. dollars	\$	\$	\$	%
Foreign exchange loss	39	Nil	39	100

Foreign exchange loss in 2004 is the result of Canadian dollar denominated expenses being paid in a period when the value of the U.S. dollar declined in relation to the Canadian dollar.

Other Expense:

	2004	2003	Change	
Stated in thousands of U.S. dollars	\$	\$	\$	%
Other expense	Nil	367	(367)	(100)

In April 2003 the Corporation paid cash of \$367,000 in final settlement of the acquisition of the Corporation's wholly owned subsidiary, Perforec. No such cost was incurred in 2004.

Income taxes:

	2004	2003	Change	
Stated in thousands of U.S. dollars	\$	\$	\$	%
Current income tax	325	146	179	123
Future income tax (reduction)	(29)	62	(91)	(147)
	296	208	88	42
Effective rate (%)	31.2	57.1		

Current income tax expense increased by 123% to \$325,000 from \$146,000 as a result of increased profitability experienced by the Corporation.

The change in future taxes to a recovery of \$29,000 in 2004 from an expense of \$62,000 in 2003 is due to the decline of the Corporation's effective tax rate in 2004 to 31.2% from 57.1% in 2003. This reflects a decrease in the Canadian statutory tax rate in 2004 and its effect on the tax assets of the Corporation, a decline in the amount of non-deductible expenses for tax purposes in Ecuador in 2004 compared to 2003, and the reclassification of Ecuadorian statutory profit-sharing provisions to operating expenses which reduced the effective Ecuadorian tax rate from 36.25% to 25%.

CONSOLIDATED FINANCIAL POSITION

Consolidated assets increased by 178% to \$33.6 million at December 31, 2004 compared to \$12.1 million at December 31, 2003. The primary reasons for the increase of \$21.5 million is the investment of \$16.4 million in property and equipment, primarily in workover and drilling rigs and related equipment, the increase in other assets of \$3.5 million and the issue of 6,153,750 common shares and 4,076,875 share purchase warrants for \$9.4 million in net proceeds.

Cash and cash equivalents decreased by 20% to \$483,000 at December 31, 2004 compared to \$600,000 at December 31, 2003. The primary reason for the slight decrease of \$117,000 is that the acquisition of \$16.4 million in property and equipment during fiscal 2004 and payout the Corporation's term loan of \$2.4 million in January 2004 consumed slightly more cash than was generated by operations combined with the \$9.4 million in net proceeds from issue of 6,153,750 common shares and 4,076,875 share purchase warrants and the cash proceeds of \$6.0 million from a shareholder loan.

Accounts receivable increased by 110% to \$4.2 million at December 31, 2004 compared to \$2.0 million at December 31, 2003. The primary reason for the increase of \$2.2 million is the increase in rig operating hours from 13,272 in the fourth quarter of 2004 compared to 8,419 in the fourth quarter of 2003.

Holdbacks and deposits receivable increased by 99% to \$670,000 at December 31, 2004 compared to \$337,000 at December 31, 2003. Because the Corporation is required on occasion to make deposits with certain clients to guarantee performance, the primary reason for the increase of \$333,000 is the timing of when projects are completed to the client's satisfaction from one period to the next which triggers the release of funds to the Corporation.

Property and equipment increased by 174% to \$24.1 million at December 31, 2004 compared to \$8.8 million at December 31, 2003. The primary reason for the increase of \$15.3 million is the \$16.4 million invested in the expansion of the Corporation's operating asset base offset by \$1.1 million in depreciation expense. Specifically, \$12.7 million has been spent during fiscal 2004 on the acquisition and construction of 3 new dual workover/drilling rigs and related equipment for deployment in Ecuador, \$2.2 million on the initial construction of drilling rigs for deployment in Venezuela, \$1.1 on the expansion of the Corporation's Ecuadorian transport fleet to 18 trucks from 10; and \$400,000 on general equipment. Two of the new dual drilling/workover rigs were deployed in the fourth quarter of fiscal 2004 in Ecuador and the third is expected to commence operations in the second quarter of fiscal 2005.

Future income tax asset increased to \$115,000 at December 31, 2004 compared to \$86,000 at December 31, 2003. The primary reason for the increase of \$29,000 is the reduction of future tax liabilities for accounting purposes in 2004.

Other assets increased to \$3.5 million at December 31, 2004 compared to a balance of \$37,000 at December 31, 2003. This increase is due primarily to the charges incurred in relation to a private placement, the funds of which were received subsequent to December 31, 2004 (note 17 to the audited consolidated financial statements). Certain charges were incurred pursuant to an Agency Agreement dated December 22, 2004 for the private placement that were comprised of \$2.3 million in cash payable (note 9 to the audited consolidated financial statements), and \$637,000 for the issue of 916,667 Broker Series III Warrants (note 10 to the audited consolidated financial statements). Additional professional fees and other costs of \$200,000 were also incurred with respect to the private placement. These costs will be reclassified as share issue costs in the period the private placement closed.

Accounts payable and accrued liabilities increased by 225% to \$5.2 million at December 31, 2004 compared to \$1.6 million at December 31, 2003. The primary reason for the increase of \$3.6 million is the increase in rig operating hours from 13,272 in the fourth quarter of fiscal 2004 compared to 8,419 in the fourth quarter of 2003, combined with the increased use of the Corporation's operating cashflow to fund capital expansion versus servicing trade credit.

The balance of the term loan payable at December 31, 2003 of \$2.4 million was paid using the proceeds of a shareholder advance in January 2004.

The balance of the advances from shareholders of \$2.1 million represents gross loan proceeds received of \$6.0 million less the conversion of \$4.2 million of the loan into 4,540,463 (1,059,000 pre-split) common shares of the Corporation at a price of \$0.93 per share (\$4.00 per share pre-split), plus accrued interest of \$281,000. The proceeds of the loan were used to retire the Corporation's term debt of \$2.4 million and assist in funding the acquisition of additional operating assets. In addition, \$615,000 of the shareholder advances payable at December 31, 2003 was also converted into 659,109 (154,000 pre-split) common shares of the Corporation at a price of \$0.93 per share (\$4.00 per share pre-split). On January 13, 2005, the Corporation repaid the balance of the shareholder advances and accordingly has classified the balance as a current liability.

Share capital increased by 243% to \$20.6 million at December 31, 2004 compared to \$6.0 million at December 31, 2003. The primary reasons for the increase of \$14.6 million are the conversion of \$4.2 million of a shareholder's loan into 4,540,463 (1,059,000 pre-split) common shares of the Corporation at a price of \$0.93 per share (\$4.00 per share pre-split), the conversion of \$615,000 of shareholder advances into 659,109 (153,707 pre-split) common shares of the Corporation at a price of \$0.93 per share (\$4.00 per share pre-split), the classification of stock-based compensation costs of \$420,000 to share capital and the issue of 6,153,750 (post-split) common shares and 4,076,875 share purchase warrants of the Corporation for net proceeds of \$9.4 million (\$9.2 million allocated to share capital and \$150,000 allocated to share purchase warrants).

The balance of share-purchase warrants increased to \$838,000 (note 10 to the audited consolidated financial statements). During fiscal 2004, the Corporation issued 5,409,712 share purchase warrants at a weighted average price of \$0.15 per warrant.

RELATED PARTY TRANSACTIONS

Conversion of Shareholder Advances:

On January 14, 2004, \$615,000 of shareholder loans was converted into 659,109 (153,707 pre-split) common shares of the Corporation at a price of \$0.93 per share (\$4.00 per share pre-split). On June 21, 2004, these shares were split on a 4.2875 to 1 basis.

Shareholder Advances:

Pursuant to a loan agreement dated January 13, 2004, a shareholder of the Corporation advanced the sum of \$6.0 million to one of the Corporation's subsidiaries. On June 21, 2004, \$4.2 million of the loan was assigned to the Corporation by its subsidiary and was immediately converted into 4,540,463 (1,059,000 pre-split) common shares of the Corporation at a price of \$0.93 per share (\$4.00 per share pre-split). On June 21, 2004, these shares were split on a 4.2875 to 1 basis.

During the year ended December 31, 2004, the Corporation incurred interest expense of \$281,000 on shareholder advances (2003 - \$36,000).

Sale of assets:

During the year ended December 31, 2004 the Corporation sold certain equipment to a Corporation with common ownership with a carrying value of \$49,000 for cash consideration of \$49,000 which was the transaction's exchange value.

CAPITAL RESOURCES AND LIQUIDITY

Selected capitalization data:

	2004	2003
Stated in thousands of U.S. dollars	\$	\$
Working capital (deficit) (1)	(2,495)	974
Current assets	5,944	3,212
Current liabilities (2)	8,439	2,238
Working capital ratio (3)	0.93	1.44
Long-term debt	Nil	2,439
Other liability (4)	2,280	Nil
Shareholder advances (current and long-term)	2,081	626
Shareholders' equity	22,894	6,800
Total debt-to-equity ratio (5)	0.19	0.45

Notes:

- (1) Calculated as current assets less current liabilities.
- (2) Includes balance of shareholder advances at December 31, 2004, which was repaid on January 13, 2005.
- (3) Calculated as current assets divided by current liabilities (excluding shareholder advances).
- (4) Paid subsequent to December 31, 2004 with proceeds from the private placement.
- (5) Calculated as long-term debt plus other liability plus shareholder advances divided by Shareholders' Equity.

Working Capital and Funds from Operations:

During the year ended December 31, 2004, the Corporation generated funds from operations of \$1.9 million an increase of 110% compared to \$905,000 for the same period in 2003. The change reflects an increase of 20% in rig operating hours to 49,523 in 2004 compared to 41,379 in 2003 combined with higher average day rates in 2004 compared to 2003.

Working capital at December 31, 2004 decreased to a deficit of \$2.5 million from a positive working capital position of \$974,000 at December 31, 2003. This decrease reflects the fact the balance of shareholder advances of \$2.1 million has been classified current liability as a result of the Corporation repaying the balance in January 2005, and that the Corporation directed all of the its cash generated from financing activities during 2004 (\$14.3 million) as well as the funds generated from operations (\$1.9 million) towards both the expansion and equipping of its rig fleet (\$16.4 million) and the repayment of its term debt (\$2.4 million).

On January 4, 2005 pursuant to an Agency Agreement dated December 22, 2004 the Corporation issued 16,666,675 units at a price of US \$2.43 per unit, for gross proceeds of US \$40.6 million. The proceeds from the private placement permitted the Corporation to repay the \$2.1 million in shareholder advances, repay the other liability of \$2.3 million, acquire an operating company in Venezuela, continue its fleet expansion plans and inject additional working capital into the Corporation.

Financing activities:

During fiscal 2004, the Corporation increased its bank debt by \$400,000 compared to a repayment of \$224,000 in 2003. This increase in bank debt utilization reflects the increase in activity during fiscal 2004 from fiscal 2003 as well as the Corporation's utilization of funds generated from operations to assist in financing the expansion and construction of the Corporation's rig fleet.

During fiscal 2004, the Corporation received gross shareholder cash advances of \$6.0 million compared to a net advance of \$535,000 in 2003.

The proceeds of the aforementioned shareholder advance received during fiscal 2004 were used to retire the Corporation's term debt in the amount of \$2.4 million and acquire additional operating assets. During fiscal 2003, the Corporation made scheduled net term debt payments of \$807,000.

During fiscal 2004, the Corporation issued 6,153,750 (post split) common shares and 4,076,875 share purchase warrants for net proceeds of \$9.4 million. No share transactions occurred in fiscal 2003. In addition, in fiscal 2004, the Corporation issued 126,481 (29,500 pre-split) common shares for net cash proceeds of \$143,000.

Investing activities:

During fiscal 2004, the Corporation invested \$16.4 million into its capital asset base compared to \$1.4 million in 2003. Specifically, \$12.7 million has been spent during fiscal 2004 on the acquisition and construction of 3 new dual workover/drilling rigs and related equipment for its Ecuador operations, \$2.2 million to commence the Corporation's fleet expansion program for its Venezuelan operations, \$1.1 million on the expansion of the Corporation's transport fleet to 18 trucks from 10; and \$400,000 on general equipment. Two of the new dual workover/drilling rigs were deployed in the fourth quarter of fiscal 2004 Ecuador and the third is expected to commence operations in the second quarter of fiscal 2005. At the conclusion of the current capital expansion program, the Corporation's Ecuadorian fleet will be comprised of 7 workover rigs and 3 dual workover/drilling rigs.

During the year ended December 31, 2004, the Corporation disposed of certain equipment for cash proceeds of \$49,000, a decrease of \$164,000 compared to proceeds of \$213,000 for the same period in 2003.

On October 21, 2004, the Corporation entered into a letter of intent to acquire all of the issued and outstanding shares of an oil and gas service company based in Venezuela. In conjunction with this letter of intent, the Corporation advanced the vendor the amount of \$200,000 which is to be applied to the purchase price upon closing. The acquisition closed on January 4, 2005. No such transaction took place in fiscal 2003. In addition, during 2004 the Corporation paid \$378,000 in other costs, comprised of \$201,000 relating to the private placement of funds and \$177,000 for professional fees related to the Venezuelan acquisition. Both the private placement and business acquisition were completed subsequent to December 31, 2004 (note 17 to the audited consolidated financial statements). These costs will be treated as a cost of financing and acquisition respectively for accounting purposes. No such transactions took place in fiscal 2003.

Financial Covenants:

As at December 31, 2004, the Corporation was in compliance with all financial covenants.

SUBSEQUENT EVENTS:

Private placement:

As disclosed in the audited consolidated financial statements, on January 4, 2005 pursuant to an Agency Agreement dated December 22, 2004 the Corporation issued 16,666,675 units at a price of \$2.43 per unit, for gross proceeds of \$40.6 million. Each unit is comprised of one common share and one-half of a share purchase warrant. Each warrant is exercisable into one common share of the Corporation at a price of \$3.11 and expire on June 30, 2006.

In conjunction with the completion of the private placement, the Corporation paid the long-term liability of \$2.3 million (note 9 to the audited consolidated financial statements).

Business acquisition:

Effective January 4, 2005 the Corporation acquired all of the issued and outstanding shares of Justiss Drilling de Venezuela S.A., a company that provides land based drilling, completions, workover and equipment rental services to major and intermediate sized oil and gas companies throughout Venezuela.

Total consideration paid was \$18.5 million consisting of \$16.9 million in cash and \$1.2 million through the issue of 402,067 common shares of the Corporation at a price per share of \$3.03. Acquisition costs relating to the transaction are estimated to be \$460,000. The acquisition will be accounted for under the purchase method and the results of operations will be included from the effective date of the acquisition.

Saxon Energy Services Inc.

The net assets acquired, at their assigned fair values are as follows:

Stated in thousands of U.S. dollars	\$
Working capital (including cash of \$555)	656
Property and equipment	19,486
Future income tax liability	(1,614)
	18,528
Consideration consisted of:	
	\$
Cash	16,850
Issue of common shares	1,218
Acquisition costs	460
	18,528

This purchase price allocation contains certain estimates and is therefore subject to change.

Acquisition of Operating Assets:

On January 18, 2005, the Corporation acquired operating assets in the United States for eventual deployment in Venezuela for consideration of \$3.1 million consisting of \$2.8 million in cash and 120,040 common shares at a price of \$3.03 per common share.

Exercise of Warrants:

Between January 1 and March 23, 2005, 1,849,612 share purchase warrants were exercised into 1,849,612 common shares of the Corporation for gross proceeds of \$4.0 million

Letter of Intent:

On March 15, 2005, the Corporation entered into a detailed letter of intent to acquire additional drilling rigs and has commenced the process for the building of additional new drilling rigs and refurbishing a further drilling rig for a total of 10 drilling rigs. These rigs will be deployed in Saxon's target geographic markets in South America. In addition, the Corporation intends to add additional complimentary rental equipment to its existing asset base. The cost of these initiatives is expected to be approximately \$74 million.

Bought Deal Private Placement:

On March 23, 2005, the Corporation entered an underwriting agreement, on a bought deal basis, with a syndicate of underwriters, pursuant to which the underwriters have agreed to purchase 16,000,000 units (the "Units") as principal on a "bought deal" basis for resale, at a price of CDN \$5.00 per Unit for gross proceeds to the Corporation of CDN \$80,000,000. The proceeds will be used to finance the Corporation's capital expansion program.

Each Unit is comprised of one half of one common share unit (the "Share Unit") of the Corporation and one half of one subscription receipt unit (the "Subscription Receipt Unit"). Each whole Share Unit consists of one common share (a "Share") and one quarter of one share purchase warrant (the "Warrant"). Each whole Subscription Receipt Unit is exchangeable for one Share and one quarter of one Warrant, for no additional consideration. Each full Warrant is exercisable into one Share on payment of CDN \$6.50 per Share for a period of twelve months from the date of closing of the offering.

One-half of the gross proceeds of this offering shall be held in escrow pending closing of the acquisition of five drilling rigs. If this acquisition has not closed on or prior to June 15, 2005, or such other date as may be agreed upon by The Corporation and the underwriters, the Corporation is obligated, out of the escrow proceeds and, if required, out of general funds of the Corporation, to refund to each holder of Subscription Receipt Units upon surrender of the Subscription Receipt Units, one-half of the subscription proceeds paid for each Unit plus a pro-rata share of the accrued interest on the escrowed funds. The offering is scheduled to close on or about April 7, 2005 and is subject to certain conditions including, but not limited to, the receipt of all necessary approvals, including the approval of the Toronto Stock Exchange.

The Corporation will pay a commission equal to 5.5% of the gross proceeds only upon receipt of the said proceeds.

FOURTH QUARTER ANALYSIS

The Corporation generated revenues of \$4.5 million for the three months ended December 31, 2004, an increase of 66% over the \$2.7 million generated during the fourth quarter of 2003. Net earnings for the three months ended December 31, 2004 was \$184,000 (\$0.01 per share) compared to a loss of \$266,000 (\$0.04 per share) in 2003. Funds generated by operations during the three months ended December 31, 2004 was \$570,000 (\$0.03 per share) compared to 2003 when operations consumed \$77,000 (\$0.01 per share) in funds.

The improvement in fiscal fourth quarter results compared to 2003 is due primarily to an increase in rig operating hours in the fourth quarter of 2004 to 13,272 compared to 8,419 in 2003, the deployment of 2 of the 3 new drilling/workover rigs in the fourth quarter of 2004 bringing the fleet to 9 operating rigs, compared to 7 in 2003 and a reduction in repairs and maintenance costs compared to the fourth quarter of 2003 when a large portion of the Corporation's existing fleet was subject to refurbishment.

NEW ACCOUNTING PRONOUNCEMENTS

The Corporation applies numerous accounting policies in preparing the Consolidated Financial Statements. From time to time, the Corporation may either revise its existing accounting policies or adopt new ones as a result of changes to how the Corporation conducts its business or due to either new or amended accounting standards as required by the Canadian Institute of Chartered Accountants (CICA).

Stock Based Compensation:

Effective January 1, 2004, the Corporation adopted the new required Canadian accounting standards that will apply the fair value method to all stock-based compensation.

Under the fair value method, the Corporation calculates the fair value of stock-based compensation and record that fair value as compensation expense over the vesting period of those grants.

CRITICAL ACCOUNTING ESTIMATES

This Management's Discussion and Analysis of the Corporation's financial condition and results of operations is based on its consolidated financial statements which are prepared in accordance with Canadian generally accepted accounting principles. The Corporation's significant accounting policies are described in Note 2 to its audited consolidated financial statements. The preparation of these financial statements requires that certain estimates and judgments be made that affect the reported assets, liabilities, revenues and expenses. These estimates and judgments are based on historical experience and on various other assumptions that are believed to be reasonable under the circumstances. Anticipating future events cannot be done with certainty, therefore these estimates may change as new events occur, more experience is acquired and as the Corporation's operating environment changes.

The accounting estimates believed to require the most difficult, subjective or complex judgments and which are the most critical to our reporting of results of operations and financial positions are as follows:

Impairment of Long-Lived Assets:

Long-lived assets, which includes property, plant and equipment and other assets, comprise a substantial portion of the Corporation's assets. The carrying value of these assets is periodically reviewed for impairment at least annually or whenever events or changes in circumstances indicate that their carrying amounts may not be recoverable. This requires the Corporation to forecast future cash flows to be derived from the utilization of these assets based upon assumptions about future business conditions and technological developments. Significant, unanticipated changes to these assumptions could require a provision for impairment in the future. As required by accounting standards, the Corporation tests its long-lived assets held for use for impairment at least annually.

Depreciation of Property Plant and Equipment:

The Corporation's operations require a significant investment in service and drilling rigs ("rigs"). In accordance with the Corporation's accounting policy related to the depreciation of property, plant and equipment, the cost of a rig is depreciated over its estimated useful life.

Judgment is involved in determining the useful life of the rigs, the estimated residual value and the appropriate method of depreciation. Factors considered in estimating the useful life of a rig include expected future usage, effects of technological or commercial obsolescence, expected wear and tear from use or the passage of time, the effectiveness of the Corporation's maintenance program and historical information of similar items retired. The accuracy in estimating the residual value of a rig becomes increasingly more difficult the further the estimated useful life extends into the future.

The Corporation's investment in rigs results in depreciation expense being a significant operating cost to the Corporation and any misjudgment in estimating the useful life or the residual value of the rigs could result in a misstatement of consolidated depreciation expense.

Allowance for Doubtful Accounts Receivable:

The Corporation performs ongoing credit evaluations of its customers and grants credit based upon past payment history, financial condition and anticipated industry conditions. Customer payments are regularly monitored and a provision for doubtful accounts is established based upon specific situations and overall industry conditions. The Corporation's history of bad debt losses has been within expectations and generally limited to specific customer circumstances, however, given the cyclical nature of the oil and gas industry and the inherent risk of successfully finding hydrocarbon reserves, a customer's ability to fulfill its payment obligations can change suddenly and without notice.

Income Tax:

The Corporation uses the liability method which takes into account the differences between financial statement treatment and tax treatment of certain transactions, assets, and liabilities. Future tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Valuation allowances are established to reduce future tax assets when it is more likely than not that some portion or all of the asset will not be realized. Estimates of future taxable income and the continuation of ongoing prudent tax planning arrangements have been considered in assessing the utilization of available tax losses. Changes in circumstances and assumptions and clarification of uncertain tax regimes may require changes to the valuation allowances associated with the Corporation's future tax assets.

BUSINESS RISK AND MANAGEMENT

The Corporation's results are affected by a number of external factors including commodity prices which drive producer capital spending levels and the demand for the Corporation's services, interest rates, and operational, credit and safety risks.

Cyclical Nature of the Oil and Gas Industry:

Demand for the Corporation's drilling services and products depends in part upon the level of oil and gas exploration and development activities conducted by oil and gas companies. Oil and gas exploration and development is highly speculative and is influenced by a variety of factors, including the prevailing prices for oil and gas which often fluctuate widely. In addition to prevailing prices for oil and gas, oil and gas exploration activity is influenced by the economic feasibility of oil and gas exploration and production, the discovery rate of new oil and gas reserves, national and international political and economic conditions and the ability of oil and gas companies to access or generate sufficient funds to finance capital expenditures for their activities.

International projects are typically longer in duration, and thereby allow for better long term planning and are less sensitive to short term product price. International projects are often driven by local political goals for energy self-sufficiency rather than profit, as is the case in North America.

The Corporation has partially managed and intends to continue to manage such risk by striving to maintain cost structures that are scalable to activity levels, and by maintaining a conservative financial structure.

The Corporation has strategically targeted its operations towards jurisdictions that are economically reliant upon the development of petroleum and natural gas reserves. This serves to insulate the Corporation from the demand cyclicity that can result from commodity price fluctuations.

Energy Services Industry Conditions and Competition:

The international energy services industry is intensely competitive, with price and reputation being the major factors in bidders being awarded contracts. The energy services industry in South and Central America continues to become more competitive. Rig availability, pricing and quality of service are the key factors affecting competitive position in these regions, but it can be expected that industry participants will continue to shift resources from Canada, the United States and other countries to these regions. The Corporation is not able to give any assurances that it can maintain its market share or level of operating profits.

Operating Risk:

The Corporation minimizes its exposure to operational risk through comprehensive vehicle and equipment maintenance programs designed to prevent failure and maximize the useful life of the related assets. In addition, The Corporation follows a complete quality assurance and control program designed to maximize performance in its work and minimize deficiencies potentially leading to failures and remedial re-work. Finally, the Corporation has a comprehensive insurance program in place designed to protect the Corporation from significant losses arising from insured events.

Foreign Operations:

During fiscal 2004, all of the Corporation's drilling and services business were generated in Ecuador. Subsequent to December 31, 2004, the Corporation completed the acquisition of an operating company located in Venezuela. Future expansion is expected to continue to maintain a significant international component. With this comes the risk of dealing with business and political systems that are significantly different from those in North America. As the Corporation grows it will strive to hire and retain employees who have experience in the international arena, recruit qualified resident nationals on the staffs of its future international operations and focus on acquisition targets with a substantial operating history in its target markets.

Impact of Government Regulations:

A significant portion of the Corporation's drilling and services business is generated either directly or indirectly by state-owned oil companies. Accordingly, a change in the funding or implementation of these programs could have an adverse effect on this segment of the Corporation's business.

The Corporation has either hired or retained personnel that have experience in working in international jurisdictions in order to mitigate these risks. In addition, the Corporation's strategy includes expansion into multiple jurisdictions so that it can readily transfer operating assets as required, thereby mitigating its exposure to country risk.

Foreign Currency Exchange Rate Risk:

A significant portion of the Corporation's international revenues and costs are expected to be generated or paid in U.S. dollars. Reported profit or loss from the Corporation's operations may be affected by changes in the exchange rate between the domestic currency and the U.S. dollar. To the extent that certain expenses are paid in local currency and revenue is earned in U.S. dollars, a weakened U.S. dollar relative to such currency would result in foreign currency exchange losses which would have a negative financial impact.

In the fiscal year ended December 31, 2004, 100% of the Corporation's operating earnings were realized from its operations in Ecuador which uses the U.S. dollar as its base currency and as such this jurisdiction has minimal currency risk.

As disclosed in the audited consolidated financial statements, subsequent to December 31, 2004, the Corporation completed the acquisition of an operating company located in Venezuela which will subject the Corporation to foreign currency exchange risk.

In Venezuela and where potential future acquisitions are located in jurisdictions where the base currency is denominated in a currency other than the U.S. dollar, the Corporation will mitigate this risk by endeavoring to structure the majority of its contracts to be paid in U.S. dollars with a portion sufficient to cover expenditures incurred locally to be paid in the local currency.

Credit Risk:

The risk of losses from customer non-payment is minimized through the Corporation's credit granting policies and other procedures designed to limit the exposure to credit risk. The Corporation has a core base of clients, the majority of which are senior producers. As a result of such practices, the Corporation's bad debt expense has historically been minimal.

Safety Risk:

Safety risks are managed through the application of safety policies and procedures conducive to promoting safe work practices to a standard either complying with or exceeding government regulations and industry requirements. The Corporation maintains a behavior-based safety program, which uses positive reinforcement to change unsafe behaviors of its employees and contractors.

Workforce Availability:

The Corporation's ability to provide reliable services is dependent upon the availability of well trained, experienced crews to operate its field equipment. The Corporation must balance the requirement to maintain a skilled workforce with the need to establish cost structures that vary as much as possible with activity levels. The Corporation's most experienced people are retained during periods of low utilization by having them fill lower level positions on our field crews. The Corporation has established training programs for employees new to the oilfield service sector and works closely with industry associations to ensure competitive compensation levels and to attract new workers to the Corporation as required.

Acquisition Integration:

The Corporation is working towards its strategic objective of becoming a significant international player in drilling and workover services in the Canadian and International marketplace. Business acquisitions will be an important tool in this pursuit. Successful integration of new businesses, people and systems will be critical to the Corporation's future success.

Merger and Acquisition Activity:

Merger and acquisition activity in the oil and gas exploration and production sector can impact demand for the Corporation's services as customers focus on reorganization activities prior to committing funds to significant drilling and work over programs. This may have a positive or negative impact on future merger and acquisitions activity and could have a short-term impact on the Corporation's business, but in the long-term should result in a stronger, more active market.

OUTLOOK

The Corporation is enthusiastic about its prospects for the upcoming fiscal 2005 year and beyond. The supply and demand fundamentals that have resulted in today's relatively high oil and natural gas price levels are not expected to change rapidly. Energy price analysts have typically focused on the supply side of the price equation where the consensus has historically been that there was sufficient supply to fill long-term demand. Continued concerns regarding the ability to increase surplus crude oil production in the Middle East combined with infrastructure concerns in the former Soviet Union brought this assertion into question during 2004. In addition, while natural gas drilling has increased significantly in recent years, this has only served to maintain gas production in the face of increasing demand.

Continued high energy prices and slower projected economic growth in Asia are expected to curtail demand growth slightly in 2005 compared to 2004. However, it is anticipated that world petroleum demand growth will exceed non-OPEC growth in supply and refining capacity during 2005 and beyond. Any real or perceived imbalance between supply and demand could cause petroleum and natural gas prices to increase further.

Producer capital spending is directly influenced by current and anticipated future crude oil and natural gas prices. Both commodities appear to have established sustainable pricing at much higher than historical levels causing industry analysts to continue to predict increasing levels of international oilfield activity for 2005 and beyond.

In addition, the oilfield service sector continues to experience increasing demand for the components and related equipment required to provide workover and drilling services to oil and gas companies. The Corporation has been very proactive by securing access to equipment and by ensuring that it has the ability to construct and assemble its equipment internally as opposed to relying on third party suppliers.

Consequently, the Corporation believes that it is well positioned to capitalize on existing market conditions and provide solid financial results to its shareholders.

Saxon Energy Services Inc.

Quarterly Financial Summary

Stated in thousands of U.S. dollars, except per share amounts	Fiscal 2004				
	Q1	Q2	Q3	Q4	Year-to-Date
Revenue	3,482	3,481	3,595	4,504	15,062
EBITDA (1)	812	527	405	671	2,415
Net earnings	346	101	21	184	652
Basic earnings per share	\$ 0.05	\$ 0.01	\$ Nil	\$ 0.01	0.05
Fully diluted earnings per share	\$ 0.05	\$ 0.01	\$ Nil	\$ 0.01	0.05
Funds from operations (2)	536	319	444	570	1,869
Weighted average shares (000's)					
Basic	7,317	9,210	18,546	20,059	13,814
Diluted	7,317	9,210	18,546	20,163	13,880

Stated in thousands of U.S. dollars, except per share amounts	Fiscal 2003				
	Q1	Q2	Q3	Q4	Year-to-Date
Revenue	3,158	3,193	2,809	2,706	11,866
EBITDA (1)	793	774	134	39	1,740
Net earnings (loss)	350	134	(62)	(266)	156
Basic earnings (loss) per share	\$ 0.04	\$ 0.02	\$ (0.01)	\$ (0.04)	\$ 0.02
Fully diluted earnings (loss) per share	\$ 0.04	\$ 0.02	\$ (0.01)	\$ (0.04)	\$ 0.02
Funds from (used in) operations (2)	541	346	95	(77)	905
Weighted average shares (000's)					
Basic	7,982	7,982	7,860	7,446	7,816
Diluted	7,982	7,982	7,860	7,446	7,816

Notes:

(1) Non-GAAP measure. See explanation on page 5.

(2) Non-GAAP measure. See explanation on page 5.

Saxon Energy Services Inc.

Management's Report to Shareholders

To the Shareholders of Saxon Energy Services Inc.

The accompanying consolidated financial statements have been approved by the Board of Directors and have been prepared in accordance with accounting principles generally accepted in Canada. The financial information presented elsewhere in this report is consistent with that shown in the accompanying consolidated financial statements.

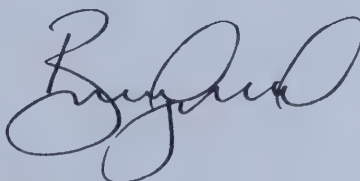
Management maintains accounting control systems designed to provide reasonable assurance that transactions are properly authorized, assets safeguarded and that the financial records form a reliable base for the preparation of accurate and timely financial information.

The Board of Directors oversees the management of the business and the affairs of the Corporation, including ensuring management fulfills its responsibilities for financial reporting and is ultimately responsible for reviewing and approving the financial statements. The Board carries out this responsibility principally through its Audit Committee.

The Audit Committee of the Board of Directors, which consists of three directors, all of which are non-management directors, has reviewed the consolidated financial statements with management and the external auditors. An independent firm of chartered accountants, appointed as external auditors by the shareholders, has audited the consolidated financial statements and its report included herein.



Walter Dawson
President and C.E.O.



Brian Orgnero
Vice President, Finance, C.F.O. and Corporate Secretary

Saxon Energy Services Inc.

Auditors' Report

To the Shareholders of Saxon Energy Services Inc.

We have audited the consolidated balance sheets of Saxon Energy Services Inc. as at December 31, 2004 and 2003 and the consolidated statements of operations and retained earnings and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 2004 and 2003 and the results of its operations and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

KPMG LLP

Chartered Accountants

Calgary, Canada

March 22, 2005

Saxon Energy Services Inc.

Balance Sheets

Expressed in U.S. Dollars

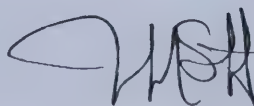
As at December 31 (stated in thousands of U.S. Dollars)	2004 \$	2003 \$
ASSETS		
Current assets		
Cash and cash equivalents	483	600
Accounts receivable	4,196	2,041
Holdbacks and deposits receivable	670	337
Supplies inventory	354	28
Prepaid expenses	241	206
	5,944	3,212
Property and equipment (note 3)	24,068	8,768
Future income tax asset (note 4)	115	86
Other assets (note 5)	3,486	37
	33,613	12,103
LIABILITIES and SHAREHOLDERS' EQUITY		
Current Liabilities		
Bank debt (note 6)	650	250
Accounts payable and accrued liabilities	5,234	1,648
Income and other taxes payable	474	250
Advances from shareholders (note 8)	2,081	-
Amounts due to related parties (note 12)	-	90
	8,439	2,238
Other liability (note 9)	2,280	-
Term loan payable (note 7)	-	2,439
Advances from shareholders (note 8)	-	626
Shareholders' Equity		
Share capital (note 10)	20,595	6,020
Share-purchase warrants (note 10)	838	-
Contributed surplus (note 10)	33	-
Retained earnings	1,428	780
	22,894	6,800
Commitments (note 15)		
Subsequent events (note 17)		
	33,613	12,103

See accompanying notes to consolidated financial statements

Approved by the Board of Directors



Walter Dawson
Director



Jeff Scott
Director

Saxon Energy Services Inc.

Statements of Operations and Retained Earnings

Expressed in U.S. Dollars

Years ended December 31 (stated in thousands of U.S. dollars)	2004 \$	2003 \$
Revenue	15,062	11,866
Expenses:		
Direct operating	10,050	8,520
General and administrative	2,180	1,583
Public listing	259	-
Stock-based compensation (note 10)	157	-
Depreciation and amortization	1,072	664
Interest on term loan	11	265
Interest on shareholder advances	281	36
Interest on bank debt	64	44
Loss on disposal of property and equipment	1	23
Foreign exchange loss	39	-
Other expense (note 13)	-	367
	14,114	11,502
Earnings before income taxes	948	364
Income taxes (note 4)		
Current	325	146
Future (reduction)	(29)	62
	296	208
Net earnings	652	156
Retained earnings, beginning of year	780	624
Net liabilities assumed on reverse-takeover (note 10(d))	(4)	-
Retained earnings, end of year	1,428	780
Net earnings per share		
Basic	\$0.05	\$0.02
Diluted	\$0.05	\$0.02

See accompanying notes to consolidated financial statements

Saxon Energy Services Inc.

Statements of Cashflows

Expressed in U.S. Dollars

Years Ended December 31 (stated in thousands of U.S. dollars)	2004 \$	2003 \$
Cash provided by (used in):		
Operating activities:		
Net earnings	652	156
Items not involving cash:		
Depreciation and amortization	1,072	664
Future income tax (reduction)	(29)	62
Stock-based compensation	157	-
Loss on disposal of property and equipment	1	23
Unrealized foreign exchange loss	16	-
Funds from operations	1,869	905
Change in non-cash working capital (note 14)	618	1,259
	2,487	2,164
Financing activities:		
Issue of share capital	9,604	-
Issue of share purchase warrants	202	-
Shareholder advances	6,025	535
Increase (decrease) in bank debt	400	(224)
Change in non-cash working capital	551	-
Repayment of long-term debt, net	(2,439)	(807)
Repayment of capital lease obligation	-	(52)
	14,343	(548)
Investing activities:		
Additions to property and equipment	(16,418)	(1,417)
Proceeds on disposal of property and equipment	49	213
Increase in other assets	(578)	(37)
	(16,947)	(1,241)
Change in cash position	(117)	375
Cash and cash equivalents, beginning of year	600	225
Cash and cash equivalents, end of year	483	600
Interest paid	75	345
Income taxes paid	250	429

See accompanying notes to consolidated financial statements

Saxon Energy Services Inc.

Notes to the Financial Statements

(Tabular amounts stated in thousands of U.S. dollars except per share amounts)

1 General:

These consolidated financial statements have been prepared by management in accordance with Canadian generally accepted accounting principles (GAAP). The preparation of financial statements in conformity with Canadian GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from these estimates.

2 Significant accounting policies:

a) Basis of presentation:

These consolidated financial statements include the accounts of the Corporation and those of its wholly-owned subsidiaries in Ecuador and Venezuela namely, Saxon Energy Services de Venezuela S.A (incorporated under the laws of Venezuela), Perforec Perforaciones Ecuatorianas S.A ("Perforec"), Santa Fe del Ecuador S.A. ("Santa Fe") and Saxon Energy Services S.A. (incorporated under the laws of the Republic of Ecuador).

b) Reporting currency:

The financial statements are expressed in United States currency, unless otherwise noted, on the basis that this is the functional currency in which the Corporation and its subsidiaries transact the substantial majority of their business.

c) Revenue recognition:

The Corporation's services are generally sold based on purchase orders or contracts with the customer that include fixed or determinable prices based upon daily, hourly or job rates. Customer contract terms do not include provisions for post-service delivery obligations. Revenue is recognized when services and equipment rentals are rendered and only when collectibility is reasonably assured.

d) Cash equivalents:

Cash equivalents consist of bank deposits and short-term investments with maturities of three months or less.

e) Supplies Inventory:

The Corporation has an inventory of supplies that are consumed in the provision of its services. This inventory is recorded at the lower of cost as determined using the first-in-first out method on a weighted average cost basis, and net realizable value. Supplies inventory is expensed as it is consumed.

f) Property and equipment:

Property and equipment is recorded at cost. Service rigs are depreciated at a rate per operating day so as to depreciate the cost, less an estimated residual value of 20%, over the operating days which the rig is expected to operate during its useful life which is 2,500 operating days. Drilling rigs are depreciated at a rate per operating day so as to depreciate the cost, less an estimated residual value of 20%, over the operating days which the rig is expected to operate during its useful life which is 3,650 operating days. Other property and equipment are depreciated on a straight-line basis over the following periods:

Assets	Period
Buildings and structures	10 to 20 years
Camp equipment	10 years
Yard and spare equipment	5 to 10 years
Automotive equipment	5 years
Office and computer equipment	5 to 10 years

Assets under construction represent drilling and workover rigs and related equipment. Depreciation will commence when the assets are put into service.

g) Impairment of long-lived assets held for use:

The Corporation is required to measure and quantify on an annual basis the amount by which the carrying amount of an asset group exceeds its fair value. Any excess of an asset group's carrying value over its fair value is considered an impairment loss and will be recognized. The fair value of an asset group is defined as the amount of consideration that would be agreed upon in an arm's length transaction between two knowledgeable parties under no compulsion to act.

h) Other assets:

Other assets represent the accumulated costs incurred regarding certain financing and business acquisition activities. Upon their successful completion these costs will be treated as a cost of financing and acquisition respectively for accounting purposes, or will be expensed if the activity is unsuccessful.

i) Income taxes:

The Corporation utilizes the asset and liability method to account for income taxes. Under this method future income tax assets and liabilities are determined based on the differences between the financial reporting and income tax bases of assets and liabilities, measured using substantially enacted income tax rates and laws that will be in effect when the differences are expected to reverse. A valuation allowance is recorded against any future income tax assets if it is more likely than not that the asset will not be realized.

j) Per share amounts:

Basic per share amounts are calculated using the weighted average number of common shares outstanding for the year. Diluted per share amounts are calculated following the treasury stock method assuming that proceeds obtained upon the exercise of warrants or options would be used to purchase common shares at the average market price during the period.

k) Share purchase warrants:

The Corporation has issued warrants to purchase common shares at a specified price in conjunction with the issue of common shares of the Corporation and as compensation to a third party for services provided. These warrants are accounted for in accordance with the fair value method of accounting, and as such the cost of the warrants is accounted for in the same manner as if the transaction was settled in cash with a corresponding amount recorded to warrants, based upon an estimate of the fair value using a Black-Scholes pricing model.

Any consideration paid on the exercise of warrants is credited to share capital. The Corporation has not incorporated an estimated forfeiture rate for warrants that will not vest; rather, the Corporation accounts for forfeitures as they occur.

l) Stock-based compensation:

The Corporation has an equity incentive plan described in note 10. Effective January 1, 2004, the Corporation adopted the Canadian accounting standard with respect to stock-based compensation, whereby, the Corporation accounts for stock options in accordance with the fair value method of accounting. Under the fair value method, the cost of the stock options is accounted for in the same manner as if the transaction was settled in cash with a corresponding amount recorded to contributed surplus, based upon an estimate of the fair value using a Black-Scholes pricing model.

Any consideration paid on the exercise of stock options is credited to share capital. The Corporation has not incorporated an estimated forfeiture rate for stock options that will not vest; rather, the Corporation accounts for forfeitures as they occur.

m) Foreign currency translation:

Assets and liabilities denominated in foreign currencies are translated into U.S. dollars at exchange rates in effect at the balance sheet date for monetary items and at exchange rates in effect at the transaction dates for non-monetary items. Income and expenses are translated at the average exchange rates in effect during the applicable period. Exchange gains or losses are included in operations in the period incurred.

n) Comparative figures:

Certain comparative figures have been reclassified to conform to the current period's presentation.

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3 Property and equipment:

	Cost	Accumulated depreciation	Net book value
	\$	\$	\$
December 31, 2004			
Land	76	-	76
Buildings and structures	138	34	104
Workover rigs	9,445	2,372	7,073
Drilling rigs	6,975	19	6,956
Workover and drilling accessories	4,424	127	4,297
Automotive equipment	1,764	346	1,418
Other	850	241	609
Assets under construction	3,535	-	3,535
	27,207	3,139	24,068
December 31, 2003			
Land	14	-	14
Buildings and structures	127	25	102
Workover rigs	9,626	1,706	7,920
Automotive equipment	433	162	271
Other	626	186	440
Assets under construction	21	-	21
	10,847	2,079	8,768

Assets under construction represent drilling and workover rigs and related equipment. Depreciation will commence when the assets are put into service.

In conducting the annual impairment test, the Corporation had a single asset group, those of its wholly-owned subsidiaries in Ecuador. The Corporation calculated fair value using discounted cash flows expected to be generated over the average economic life of those assets and determined that the fair value of that asset group exceeded its carrying value and as such no impairment exists as at December 31, 2004.

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4 Future income taxes:

To date the Corporation's operations have been carried out almost exclusively in Ecuador. Under Ecuadorian law the Corporation's subsidiaries are subject to corporate income tax at a rate of 25%. Income tax expense differs from the expected amount, calculated at the combined Canadian federal and provincial statutory rate, as set out below:

	2004 \$	2003 \$
Earnings before income taxes	948	364
Combined federal and provincial income tax rate	33.87%	37.12%
Expected income tax provision	321	135
Non-deductible foreign expenses	54	128
Non-deductible stock-based compensation expense	53	-
Loss on disposal of property and equipment	1	8
Difference between Canadian and Ecuadorian statutory rate	(124)	(56)
Adjustments for enacted changes in income tax rates	(9)	(7)
	296	208

The components of the net income tax asset are as follows:

	2004 \$	2003 \$
Property and equipment	(117)	(67)
Income tax losses	232	153
Share Issue costs	1,101	-
Valuation allowance	(1,101)	-
	115	86

Income tax losses for Canadian tax purposes of approximately \$725,053 are available to reduce or eliminate income otherwise taxable in the future. These losses expire commencing in 2007.

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5 Other assets:

December 31, 2004	2004 \$	2003 \$
Financing charges	3,109	37
Business acquisition costs	177	-
Deposit on acquisition	200	-
	3,486	37

Financing charges include costs incurred pursuant to an Agency Agreement dated December 22, 2004, related to a private placement which closed subsequent to December 31, 2004 (note 17) and are primarily comprised of agent's commission and the issuance of broker warrants (note 9).

Business acquisition costs are primarily composed of professional fees related to the business acquisition that closed subsequent to December 31, 2004 (note 17). These costs will be recorded to the respective financing or business acquisition costs at the time of closing.

On October 21, 2004, the Corporation entered into a letter of intent to acquire all of the issued and outstanding shares of an oil and gas service company incorporated and operating in Venezuela. In conjunction with this letter of intent, the Corporation advanced the vendor the amount of \$200,000 which is to be applied to the purchase price upon closing. The acquisition closed on January 4, 2005 (note 17).

6 Bank debt:

As at December 31, 2004, the Corporation had demand revolving lines of credit totaling \$650,000 (December 31, 2003: \$250,000).

The lines of credit bear interest at between 10% to 12% annually, are secured by certain accounts receivable, and property and equipment of the Corporation and have a total available draw of \$729,000.

7 Term loan payable:

The balance of the term loan payable of \$2.2 million plus accrued interest of \$265,000 at December 31, 2003 was repaid in January 2004 using the proceeds of shareholder advances (note 8), a portion of which was subsequently exchanged for common shares (note 10). The term loan was secured by certain property and equipment of the Corporation and carried interest at 9% annually, with principle and interest payments payable quarterly.

8 Advances from shareholders:

Pursuant to a loan agreement dated January 13, 2004, a shareholder of the Corporation advanced the sum of \$6.0 million due January 14, 2006 bearing interest at 10% annually (2003 - 9% annually) and is secured by certain property and equipment of the Corporation (2003 - unsecured). On June 21, 2004, \$4.2 million of the loan balance was exchanged for common shares of the Corporation (see note 10). During the year ended December 31, 2004 the Corporation accrued interest on the shareholder advances of \$281,000 (2003: \$36,000). On January 13, 2005, the Corporation repaid the outstanding balance of \$1.8 million plus accrued interest and accordingly, the balance of advances from shareholder have been classified as a current liability.

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9 Other liability:

Pursuant to an Agency Agreement dated December 22, 2004, the Corporation has committed to paying agents acting in the capacity of financial advisor fees, payable in cash, equal to 5.5% of the proceeds of a private placement, the proceeds of which were received subsequent to December 31, 2004 (note 17), and issuing broker warrants equal to 5.5% of the total units issued by the Corporation pursuant to the same private placement (note 10).

Consequently, the Corporation has recorded a liability equal to the cash fees payable of \$2.3 million with a corresponding increase to other assets. Subsequent to December 31, 2004 the Corporation received the funds from the private placement (note 17) and accordingly, the Corporation has classified the corresponding liability as long term.

10 Share capital:

a) Authorized:

- i) Unlimited number of voting Common Shares
- ii) Unlimited number of non-voting Preferred Shares, issuable in series

b) Issued:

	Preferred Shares		Common Shares		Total Amount \$
	Number	Amount \$	Number	Amount \$	
Balance December 31, 2003 and 2002	1,861,672	6,020	2	-	6,020
Conversion of Preferred Shares into Common Shares	(1,861,672)	(6,020)	1,861,672	6,020	-
Issued on conversion of portion of shareholder advances	-	-	153,707	615	615
Issued for cash	-	-	29,500	143	143
Issued on conversion of portion of shareholder loan	-	-	1,059,000	4,236	4,236
Effect of 4.2875:1 share split	-	-	10,204,119	-	-
Private placements of units net of issue costs of \$997,782	-	-	6,153,750	9,159	9,159
Issued for services rendered	-	-	210,000	422	422
Issued on reverse-takeover transaction	-	-	1,019,086	-	-
Balance December 31, 2004	-	-	20,690,836	20,595	20,595

- i) On January 14, 2004, 1,861,672 Series A Preferred Shares were exchanged for 1,861,672 common shares at a price of \$3.23 (pre-split) per share (\$0.75 per share post-split), for total consideration of \$6.0 million. On November 26, 2004 pursuant to the reverse-takeover transaction (note 10(d)), all of the authorized Series A Preferred shares were cancelled.
- ii) On January 14, 2004, \$615,000 of shareholder loans were exchanged for 153,707 common shares at a price of \$4.00 (pre-split) per common share (\$0.93 per share post-split).
- iii) On March 26, 2004 and April 30, 2004, the Corporation issued 25,000 and 4,500 common shares respectively at a price per common share of \$4.00 (pre-split) and \$5.00 (pre-split) respectively (\$0.93 and \$1.17 per share post-split, respectively) for total consideration of \$143,000.
- iv) On June 21, 2004, the Corporation converted a shareholder loan in the amount of \$4.2 million into 1,059,000 common shares at a price per common share of \$4.00 (pre-split) (\$0.93 per share post split).
- v) On June 21, 2004, the Corporation split its 3,103,881 outstanding common shares on a 4.2875 to 1.0 basis into 13,308,000 Common Shares.
- vi) Between June 30 and August 30, 2004, pursuant to Agency Agreements dated June 30, 2004 and July 8, 2004, the Corporation issued 6,153,750 units for gross proceeds of \$10.3 million as follows:

2,000,000 units at \$1.50 per unit for gross cash proceeds of \$3.0 million (\$2.9 million allocated to common shares and \$80,000 allocated to warrants). Each unit is comprised of one common share of the Corporation and one Series I Share Purchase Warrant. Each Series I Share Purchase Warrant is exercisable into one common share at a price of \$2.00 per Common Share by April 29, 2005.

2,500,000 units at \$1.60 per unit for gross cash proceeds of \$4.0 million (\$4.0 million allocated to common shares and \$12,000 allocated to warrants). Each unit is comprised of one common share of the Corporation and one-half Series II Share Purchase Warrant. Each whole Series II Share Purchase Warrant is exercisable into one common share at a price of \$2.75 per common share by August 30, 2005.

1,653,750 units at \$2.00 per unit for gross cash proceeds of \$3.3 (\$3.2 million allocated to common shares and \$58,000 allocated to warrants). Each unit is comprised of one Common Share of the Corporation and one-half Series II Share Purchase Warrant. Each whole Series II Share Purchase Warrant is exercisable into one common share at a price of \$2.75 per common share by August 30, 2005.

- vii) In conjunction with the private placements completed between June 30 and August 30, 2004, the Corporation incurred share issue costs of \$650,000 paid in cash, \$300,000 on the issue of shares for services rendered (note 10(c)), and \$48,000 on the issue of broker warrants (note 10(e))

c) Shares issued for services rendered

Between July 1 and August 30, 2004, the Corporation issued 210,000 Common Shares from treasury at a price of \$0.01 per share for gross cash proceeds of \$2,000. These shares were primarily issued as compensation to certain parties for the recruitment of investment capital into the Corporation.

The Corporation has estimated the fair value of the 210,000 Common Shares to be \$2.00 per share. The Corporation has recorded the fair value as follows: a charge of \$300,000 to share issue costs, \$120,000 to stock-based compensation expense, and a credit to share capital of \$420,000.

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d) Reverse-takeover amalgamation:

On November 26, 2004, the Corporation entered into a reverse-takeover amalgamation (the "Amalgamation") transaction with Consolidated Epix Technologies Limited ("Epix"), a reporting issuer on the TSX Venture Exchange with the successor company ("Amalco") to be named Saxon Energy Services Inc.

Pursuant to the Amalgamation, the common shares of Epix were exchanged for common shares of Amalco on a 3 for 1 basis resulting in the issue of 1,019,086 common shares of Amalco.

The issued and outstanding common shares of the Corporation as of November 26, 2004 were exchanged for common shares of Amalco on a 1 for 1 basis resulting in the issue of 19,671,750 common shares of Amalco.

The total number of common shares of Amalco outstanding subsequent to the Amalgamation was 20,690,836.

All outstanding share purchase warrants of the Corporation were exchanged on a 1 to 1 basis for share purchase warrants of Amalco. This resulted in the Issue of 2,000,000 Amalco Series I Warrants exercisable at \$2.00 per common share, 2,076,875 Amalco Series II Warrants exercisable at \$2.75 per common share, 158,319 Amalco Broker Series I Warrants exercisable at \$1.50 per common share, and 257,851 Amalco Broker Series II Warrants exercisable at \$2.00 per common share, including 50,000 Amalco Broker Series II Warrants which were issued upon completion of the transaction.

In conjunction with the Amalgamation, the Corporation acquired cash of \$2,000 and assumed net current liabilities of \$6,000, resulting in a net charge to retained earnings of \$4,000.

In conjunction with the Amalgamation, Amalco applied for and received approval to list its issued and outstanding shares on the Toronto Stock Exchange.

e) Share purchase warrants:

	Per Share Exercise Price	Outstanding Share Purchase Warrants	Weighted Fair Value Per Warrant \$	Amount \$
Balance December 31, 2003	-	-	-	-
Issue of Series I Share Purchase Warrants	\$2.00	2,000,000	0.04	80
Issue of Series II Share Purchase Warrants	\$2.75	2,076,875	0.03	70
Issue of Broker Series I Share Purchase Warrant	\$1.50	158,319	0.21	33
Issue of Broker Series II Share Purchase Warrants	\$2.00	207,851	0.07	15
Issue of Broker Series II Share Purchase Warrants	\$2.00	50,000	0.07	3
Issue of Broker Series III Share Purchase Warrants	\$2.49	916,667	0.69	637
Balance December 31, 2004		5,409,712	0.15	838

- i) The Corporation issued share purchase warrants pursuant to Agency Agreements dated June 30, 2004 and July 8, 2004. The Corporation calculated the fair value of warrants using the Black-Scholes pricing model to estimate the fair value of the warrants issued at the date of grant. Each series of warrants was valued using a risk-free interest rate of 4.2%; and volatility of 30%. The fair value of each series of warrants was accounted for as follows:

2,000,000 Series I Warrants and 2,076,875 Series II Warrants which are exercisable into one common share of the Corporation at \$2.00 and \$2.75 per common share respectively. These Warrants expire August 5, 2005.

The fair value of warrants issued of \$80,000 (Fair Value of \$0.04 per Series I Warrant) and \$70,000 (Fair Value of \$0.03 per Series II Warrant) respectively has been accounted for as a reduction to share capital with a corresponding increase in the amount of warrants.

158,319 Broker Series I Warrants exercisable into one common share of the Corporation at a price of \$1.50 per common share and 207,851 Broker Series II Warrants exercisable into one common share of the Corporation at a price of \$2.00 per common share. Both Broker Series Warrants expire November 26, 2005.

The fair value of warrants issued of \$33,000 (Fair Value of \$0.21 per Broker Series I Warrant) and \$15,000 (Fair Value of \$0.07 per Broker Series II Warrant) respectively has been accounted for as share issue expense in share capital with a corresponding increase in the amount of warrants.

50,000 Broker Series II Warrants exercisable into one common share of the Corporation at a price of \$2.00 per common share. The Broker Series II Warrants expire November 26, 2005.

The fair value of warrants issued of \$3,000 (Fair Value of \$0.07 per Broker Series II Warrant) has been accounted for as stock-based compensation expense with a corresponding increase in the amount of warrants.

- ii) Pursuant to an Agency Agreement dated December 22, 2004 the Corporation issued 916,667 Broker Series III Warrants equal to 5.5% of the total units issued by the Corporation pursuant to a private placement, the funds of which were received subsequent to December 31, 2004 (note 17). Each broker warrant is exercisable into one common share of the Corporation at a price of \$2.49 per share by June 30, 2006.

The Corporation calculated the fair value of the Broker Series III Warrants using the Black-Scholes pricing model to estimate the fair value of the warrants issued at the date of grant. The warrants were valued using a risk-free interest rate of 4.2%; and volatility of 70%. The fair value of warrants issued of \$637,000 (Fair Value of \$0.69 per Broker Series III Warrant) has been accounted for as deferred financing charges (note 5).

f) Stock option plan:

Pursuant to a Stock Option Plan (the "Plan"), the Board of Directors of the Corporation (the "Board") may allocate non-transferable options to purchase common shares to directors, officers and employees ("Insiders") of the Corporation and to consultants retained by the Corporation. Under the Plan, 4,138,168 shares have been reserved and set aside for issue, with the Board having the right from time to time to increase this number, subject to shareholder and regulatory approval.

Under the terms of the Plan, the maximum number of shares that may be reserved for issuance to Insiders is ten percent of the issued and outstanding shares, while the maximum number of shares which may be issued to Insiders under the plan within a one year period shall be ten percent of the issued and outstanding shares at the time of grant. Furthermore, the maximum number of shares which may be reserved for issuance to any one person under the plan

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shall be five percent of the issued and outstanding shares, while the maximum number of shares which may be issued to any one insider is five percent of the issued and outstanding shares at the time of grant.

A summary of the status of the Corporation's stock option plan as at December 31, 2004 and the changes during the year is presented below:

	Outstanding Options	Weighted average exercise price	Option expiry date	Options exercisable
Balance December 31, 2003	-	-	-	-
Stock options granted	1,675,000	2.44	December 19, 2009	-
Balance December 31, 2004	1,675,000	2.44	December 19, 2009	-

The Corporation calculated the fair value of the stock options granted using the Black-Scholes pricing model to estimate the fair value of the stock options issued at the date of grant. The weighted average fair market value of the warrants and the assumptions used in their determination are as follows: Weighted average fair value per option: \$1.80; risk-free interest rate: 4.2%; and volatility: 70%. The fair value of stock options issued on December 20, 2004 of U.S. \$33,000 has been accounted for as stock-based compensation expense with a corresponding increase in the amount of contributed surplus.

11 Financial instruments:

a) Credit risk:

In most cases the Corporation's customers are well-established and well-financed entities in the oil industry such that the level of credit risk is limited.

The Corporation had two customers which accounted for 44% and 38% of revenues respectively during the year ended December 31, 2004 (year ended December 31, 2003: 51% and 44% respectively). The amounts receivable from these customers at December 31, 2004 was \$1.3 million and \$1.1 million respectively (December 31, 2003: \$620,000 and \$724,000 respectively).

b) Fair values:

The fair values of all current monetary assets and liabilities approximate their carrying values due to the relatively short periods to maturity of these instruments. It was not considered practicable to estimate the fair values of either long-term debt or the advances from shareholders.

12 Related party transactions:

a) Sale of assets:

During the year ended December 31, 2004 the Corporation sold certain equipment to a company with common ownership with a carrying value of \$49,000 for cash consideration of \$49,000 which was the transaction's exchange value.

b) Related party balances:

As at December 31, 2004 there were no significant amounts owed to related parties (December 31, 2003: \$90,000). The 2003 balance represents amounts owed to a company with common ownership that made purchases from third party vendors on behalf of the Corporation. The balance did not bear interest and was unsecured.

13 Other expense:

In settlement of certain items related to the acquisition of the Corporation's wholly owned subsidiary, Perforec, in April 2003 the Corporation paid cash of \$367,000.

14 Changes in non-cash working capital:

The changes in non-cash working capital are as follows:

Year Ended December 31	2004 \$	2003 \$
Accounts receivable	(2,155)	851
Holdbacks and deposits receivable	(333)	246
Supplies inventory	(326)	(16)
Prepaid expenses	(35)	41
Accounts payable and accrued liabilities	3,333	418
Income taxes payable	224	(179)
Amounts due to related parties	(90)	(102)
	618	1,259

15 Commitments:

- a) The Corporation has entered into a premises lease agreement dated October 1, 2002 to lease certain property and office space located in Quito, Ecuador. The agreement is renewable annually and has a fixed monthly installment of U.S. \$2,000.
- b) The Corporation has entered into a premises lease agreement dated July 1, 2004 to lease certain property and office space located in Calgary, Canada. The agreement may be cancelled by either party with sixty days prior notice and has a fixed monthly installment of \$2,000 plus operating costs.

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16 Segmented information:

The Corporation currently operates in one geographic segment and one industry segment. During fiscal 2004 the Corporation operated an oil and gas drilling, servicing and equipment rental business in Ecuador.

2004	Ecuador	Corporate & other	Total
Revenue	15,062	-	15,062
Earnings (loss) before income taxes	1,758	(810)	948
Depreciation and amortization	1,064	8	1,072
Interest on term loan	11	-	11
Interest on shareholder advances	281	-	281
Interest on bank debt	86	(22)	64
Property and equipment	20,516	17	20,533
Assets under construction	1,304	2,231	3,535
Total property and equipment	21,820	2,248	24,068
2003			
Revenue	11,866	-	11,866
Earnings (loss) before income taxes	489	(125)	364
Depreciation and amortization	664	-	664
Interest on term loan	265	-	265
Interest on shareholder advances	-	36	36
Interest on bank debt	44	-	44
Property and equipment	8,747	-	8,747
Assets under construction	21	-	21
Total property and equipment	8,768	-	8,768

17 Subsequent events:

a) Private placement:

On January 4, 2005, pursuant to an Agency Agreement dated December 22, 2004, the Corporation received the proceeds from the issue of 16,666,675 units at a price of \$2.43 per unit, for gross proceeds of \$40.6 million. Each unit is comprised of one common share and one-half of a share purchase warrant. Each warrant is exercisable into one common share of the Corporation at a price of \$3.11 and expires by June 30, 2006.

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b) Business acquisitions:

Effective January 4, 2005 the Corporation acquired all of the issued and outstanding shares of Justiss Drilling de Venezuela S.A., a company that provides land based drilling, completions, workover and equipment rental services to major and intermediate sized oil and gas companies throughout Venezuela

Total consideration paid was \$18.5 million consisting of \$16.9 in cash and \$1.2 million through the issue of 402,067 common shares of the Corporation at an agreed price of \$3.03 per share. Acquisition costs relating to the transaction are estimated to be \$460,000. The acquisition will be accounted for under the purchase method and the results of operations will be included from the effective date of the acquisition.

The net assets acquired, at their assigned fair values are as follows:

	\$
Working capital (including cash of \$555)	656
Property and equipment	19,486
Future income tax liability	(1,614)
Consideration	18,528
Consideration consisted of:	
	\$
Cash	16,850
Issue of common shares	1,218
Acquisition costs	460
	18,528

This purchase price allocation contains certain estimates and is therefore subject to change.

c) Acquisition of operating assets:

On January 18, 2005, the Corporation acquired operating assets in the United States for eventual deployment in Venezuela for consideration of \$3.1 million consisting of \$2.8 million in cash and 120,040 common shares at an agreed price of \$3.03 per common share.

d) Exercise of share purchase warrants:

Between January 1 and March 23, 2005, 1,849,612 share purchase warrants were exercised into 1,849,612 common shares of the Corporation for gross proceeds of \$4.0 million.

e) Letter of intent:

On March 15, 2005, the Corporation entered into a detailed letter of intent to acquire additional drilling rigs and has commenced the process for the building of additional new drilling rigs and refurbishing a further drilling rig for a total of 10 drilling rigs. These rigs will be deployed in Saxon's target geographic markets in South America. In addition, the Corporation intends to add additional complimentary rental equipment to its existing asset base. The cost of these initiatives is expected to be approximately USD \$74 million.

f) Private placement:

On March 23, 2005, the Corporation entered an underwriting agreement, on a bought deal basis, with a syndicate of underwriters, pursuant to which the underwriters have agreed to purchase 16,000,000 units (the "Units") as principal on a "bought deal" basis for resale, at a price of CDN \$5.00 per Unit for gross proceeds to the Corporation of CDN \$80,000,000. The proceeds will be used to finance the Corporation's capital expansion program (note 17(e)).

Each Unit is comprised of one half of one common share unit (the "Share Unit") of the Corporation and one half of one subscription receipt unit (the "Subscription Receipt Unit"). Each whole Share Unit consists of one common share (a "Share") and one quarter of one share purchase warrant (the "Warrant"). Each whole Subscription Receipt Unit is exchangeable for one Share and one quarter of one Warrant, for no additional consideration. Each full Warrant is exercisable into one Share on payment of CDN \$6.50 per Share for a period of twelve months from the date of closing of the offering.

One-half of the gross proceeds of this offering shall be held in escrow pending closing of the acquisition of 5 drilling rigs. If this acquisition has not closed on or prior to June 15, 2005, or such other date as may be agreed upon by The Corporation and the underwriters, the Corporation is obligated, out of the escrow proceeds and, if required, out of general funds of the Corporation, to refund to each holder of Subscription Receipt Units upon surrender of the Subscription Receipt Units, one-half of the subscription proceeds paid for each Unit plus a pro-rata share of the accrued interest on the escrowed funds. The offering is scheduled to close on or about April 7, 2005 and is subject to certain conditions including, but not limited to, the receipt of all necessary approvals, including the approval of the Toronto Stock Exchange.

The Corporation will pay a commission equal to 5.5% of the gross proceeds only upon receipt of the said proceeds.

Saxon Energy Services Inc.

CORPORATE INFORMATION

Directors

Walter Dawson

Chairman

Calgary, Alberta

Jeffrey Scott

Director

Calgary, Alberta

John Rooney

Director

Calgary, Alberta

Alex Kabatoff

Director

Calgary, Alberta

Doug Paul

Director

Lethbridge, Alberta

Officers

Walter Dawson

President, Chief Executive Officer

Brian Orghero

Vice-President, Finance, Chief Financial

Officer and Corporate Secretary

Jim Howdle

Vice-President, Operations

Randy Pounds

Vice-President, International Operations

Enrique Munoz Pinilla

Vice-President, Finance Latin America

Legal Counsel

Miles Davison, LLP

Barristers & Solicitors

Calgary, Alberta

Auditors

KPMG LLP

Calgary, Alberta

Banker

HSBC Bank of Canada

Calgary, Alberta

Stock Exchange Listing

The Toronto Stock Exchange

Symbol: SES

Transfer Agent

Equity Transfer Services Inc.

Toronto, Ontario, Canada

Website

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